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In the Supreme Court of the United States

OCTOBER TERM, 1929

NEW YORK LIFE INSURANCE COMPANY, PETITIONER

v.

FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE FOR THE SECOND DISTRICT OF THE STATE OF NEW YORK

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

In the Supreme Court of the United States

OCTOBER TERM, 1929

No. 851

NEW YORK LIFE INSURANCE COMPANY, PETITIONER

v.

FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE for the Second District of the State of New York

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

The respondent does not oppose the granting of the petition for a writ of certiorari in the above-entitled case.

The questions raised by the petition are of public importance. The Government is submitting to this Court a petition for a writ of certiorari to review that part of the judgment below which was favorable to the petitioner herein. In order that all of the questions may be considered together, the Government does not oppose the present petition.

THOMAS D. THACHER,
Solicitor General.

CLAUDE R. BRANCH,
Special Assistant to the Attorney General.

MAY, 1930.

U. S. GOVERNMENT PRINTING OFFICE: 1930

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Supreme Court of the United States.

OCTOBER TERM, 1930.

No. 93.

NEW YORK LIFE INSURANCE COMPANY, Petitioner,

vs.

FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE FOR THE SECOND DISTRICT OF THE STATE OF NEW YORK.

No. 160.

FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE FOR THE SECOND DISTRICT OF THE STATE OF NEW YORK, Petitioner,

vs.

NEW YORK LIFE INSURANCE COMPANY.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR PETITIONER IN No. 93 AND FOR RESPONDENT IN No. 160.

JAMES H. McINTOSH,
Attorney for Petitioner in No. 93
and for Respondent in No. 160,
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THE BALLOU PRESS NEW YORK

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Supreme Court of the United States.

OCTOBER TERM, 1930.

NEW YORK LIFE INSURANCE COMPANY, Petitioner, vs. FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE FOR THE SECOND DISTRICT OF THE STATE OF NEW YORK,	No. 93.
FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE FOR THE SECOND DISTRICT OF THE STATE OF NEW YORK, Petitioner. vs. NEW YORK LIFE INSURANCE COMPANY.	No. 160

BRIEF FOR PETITIONER IN No. 93 AND FOR RESPONDENT IN No. 160.

Brief Statement of the Issue.

MAY IT PLEASE THE COURT,—

This is an action to recover capital stock taxes assessed in October, 1922 (R. 38), under Section 1,000 of the Revenue Act of 1918, and paid under protest November 4, 1922 (R. 39), for the years ending June 30, 1919, June 30, 1920, June 30, 1921, and June 30, 1922.

A jury was waived in writing pursuant to the statute (R. 36) and the case tried by the Court upon an agreed statement of facts which it was agreed should be treated as special findings of fact by the Court (R. 36), but which, as a matter of precaution, was put into the form of a bill of exceptions which was settled, allowed and filed as such (R. 36, 174).

The case involves two questions,—

FIRST. How many years' taxes may be collected under a revenue act which was approved February 24, 1919 (U. S. Statutes At Large, Vol. 40, Part I, p. 1152, Section 503) and ceased January 1, 1921, to be effective as to corporations such as the plaintiff (Revenue Act of 1921, U. S. Statutes At Large, Vol. 42, p. 219, Sections 243 and 263)? That is, may taxes be assessed and collected for four years under a statute that was passed February 24, 1919, and ceased to be effective twenty-two months and seven days thereafter? Both courts held, but each on different grounds, that three years was the longest period under which taxes could be collected under the Act; and the court's judgment for the plaintiff for the return of the taxes paid for the year ending June 30, 1922, is the basis of the Collector's Writ of Certiorari in No. 160. The company claims that no capital stock tax was collectable for the year ending June 30, 1921, or for the year ending June 30, 1922, because the Revenue Act of 1921 imposed on the company for 1921 and thereafter a special income tax and expressly stated that the special income tax so imposed was in lieu of the capital stock tax (Revenue Act of 1921, Section 243, U. S. Statutes At Large, Vol. 42, p. 261).

SECOND. Are sums (1) which have been declared as dividends and are payable to policyholders on the anniversary of their insurance during the current year, whether the premiums then due are paid or not (R. 47), and (2) the difference between the amount of premium paid by the policyholder and the actual cost of his insurance as later ascertained, which is "held by the company awaiting apportionment among and payment to its deferred dividend policyholders (R. 42)" surplus or contingent reserves *maintained*

for the general use of the business? Or are these sums liabilities of the company which should be deducted in calculating the net value of its property in ascertaining the sum upon which the capital tax may be assessed? Both courts held that these items were "surplus or contingent reserves maintained for the general use of the business." The company claims they are fixed liabilities of the company payable to its policyholders; that neither of them is maintained for the general use of the business; and that in addition to this the latter item is specifically excluded by that paragraph (b) of the law which says,—

> "(b) In computing the tax in the case of insurance companies such deposits * * * as they are required * * * by * * * contract to * * * hold * * * for payment to or apportionment among policyholders shall not be included."

Official Report of Opinions Delivered.

The Trial Court's opinion is found in 34 Fed. (2d) 945 and in the record commencing at page 27.

The Circuit Court of Appeals' opinion is found in 39 Fed. (2d) 556, and in the record commencing at page 184.

Grounds of the Court's Jurisdiction.

(1) Date of Trial Court's Judgment, June 27th, 1929 (R. 36). Date of Circuit Court of Appeals' judgment March 10th, 1930 (R. 192).

(2) This is a civil suit arising under a law providing for internal revenue, to wit, under the Revenue Act of 1918, entitled "An Act to Provide Revenue, and for other purposes, approved February 24, 1919" (40 U. S. Statutes At Large, 1057), and especially arises under Section 1000, Title X, of that Act, page 1126. The Commissioner assessed the tax for the four years all at one time in October, 1922 (R. 38). The Company paid them at one time, November 4, 1922 (R. 39),

and filed its claim for refund November 23, 1922 (R. 40), which was rejected by the Commissioner March 31, 1923 (R. 39). Thereupon the company commenced this suit April 28, 1923, to recover the taxes so paid (R. 1). The case involves the construction and application of Section 1000 of the Revenue Act of 1918. It is here on Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

(3) The statutory provisions under which jurisdiction is invoked are the Judicial Code, Section 24, Sub-paragraph Fifth, and Section 240 as amended.

The Capital Stock Tax Law.

Section 1000 of the Revenue Act of 1918, with the parts of it important to this case printed in italics, is as follows,—

"Sec. 1000. (a) That on and after July 1, 1918, in lieu of the tax imposed by the first subdivision of Section 407 of the Revenue Act of 1916—

(1) Every domestic corporation shall pay annually a special excise tax with respect to carrying on or doing business, equivalent to $1 for each $1,000 of so much of the fair average value of its capital stock for the preceding year ending June thirtieth as is in excess of $5,000. In estimating the value of capital stock the surplus and undivided profits shall be included;

(2) Every foreign corporation shall pay annually a special excise tax with respect to carrying on or doing business in the United States, equivalent to $1 for each $1,000 of the average amount of capital employed in the transaction of its business in the United States during the preceding year ending June thirtieth.

(b) *In computing the tax in the case of insurance companies such deposits* and reserve funds *as they are required by* law or *contract to* maintain or *hold for* the protection of or *payment to or apportionment among policyholders shall not be included.*

(c) *The taxes imposed by this section shall not apply in any year to any corporation which was not engaged in*

business (or in the case of a foreign corporation not engaged in business in the United States) *during the preceding year ending June 30,* nor to any corporation enumerated in Section 231. *The taxes imposed by this section shall apply to mutual insurance companies, and in the case of every such domestic company the tax shall be equivalent to $1 for each $1,000 of the excess over $5,000 of the sum of its surplus or contingent reserves maintained for the general use of the business and any reserves the net additions to which are included in net income under the provisions of Title II,* (The Income Tax) as of the close of the preceding accounting period used by such company for purposes of making its income tax return; Provided, that in the case of a foreign Mutual Insurance Company the tax shall be equivalent to $1 for each $1,000 of the same proportion of the sum of such surplus and reserves, which the reserve fund upon business transacted within the United States is of the total reserve upon all business transacted, as of the close of the preceding accounting period used by such company for purposes of making its income tax return.

(d) Sec. 257 shall apply to all returns filed with the Commissioner for purposes of the tax imposed by this section."

STATEMENT OF THE CASE.

I.

The nature of the company and its business, the levy and collection of the taxes in dispute, and the foundation of this action.

1. The plaintiff (herein called the Company) a New York corporation (R. 37), "is a mutual company transacting the business of life insurance on the purely mutual level premium plan * * * and has not, and never has had, any capital stock or stockholders (R. 37)".

2. The Company duly made and filed its capital stock tax return for each of the several years ending June 30, 1919, June 30, 1920, June 30, 1921 and June 30, 1922 (R. 38). Each of these returns showed no capital stock tax payable (R. 38). The Company made its returns in good faith, believing that each of them was full, complete and true (R. 38). Thereafter, and in October, 1922, the Commissioner made a final audit of the Company's returns and calculated its capital stock value for the purpose of the tax for the year ending June 30, 1919, to be $124,500,000; for the year ending June 30, 1920, $117,019,000; for the year ending June 30, 1921, $108,275,000; for the year ending June 30, 1922, $94,134,000 (R. 38); and he assessed a tax thereon accordingly which the Company paid under protest November 4, 1922 (R. 39).

This was a new and, to me at least, a startling disclosure "of the fair average value of the capital stock" of any life insurance corporation, stock or mutual, anywhere, any time. Surely there must be something wrong with these gigantic sums.

3. After paying the taxes under protest November 4, 1922, the Company, November 23, 1922, filed its claim for refund,

which the Commissioner rejected March 31, 1923 (R. 39); and thereupon, April 28, 1923 (R. 1) the Company commenced this suit.

II.

A corporation without capital stock may be taxed on the same basis as corporations with capital stock by imposing the tax on the net value of the property owned by it and used in its business. This is what Congress intended to do by this Act.

The Department itself seems to have regarded the net assets of a corporation to be substantially the measure of the value of the capital stock for the purpose of this tax, for in Regulation 64, Article 15, the Department says,—

> "If the market value of the assets be established, the fair value of the capital stock is held to be not materially less than the fair market value of the net assets."

In fact in the case of the Massachusetts Trusts this Court approved net assets as a proper way of taxing under this law concerns which have no fixed share capital.

Hecht v. *Malley*, 265 U. S. 144.

These trusts had no share capital. The Commissioner assessed them "by taking the fair value of the assets of the association over its liabilities and calling the difference its capital stock." The Court said a tax on its net assets is the way a concern without share capital should be taxed under this law. But, net assets are the same thing as "surplus or contingent reserves maintained for the general use of the business."

Indeed, in an opinion published May 1, 1922, the Solicitor of the Department laid down the following rules for taxing mutual insurance companies under this Act,—

"In determining the amount of the assets upon which the capital stock is to be assessed, there should be deducted from the total assets the following amounts,—

(1) The debt liabilities;

(2) The legal reserves;

(3) Such percentage of the amount of shrinkage from the total value of the assets to the market value of the assets as the amount of the assets in excess of the legal reserves bears to the total assets."

Internal Revenue Bulletin, Vol. 1, No. 18, May 1, 1922, page 37.

Why the Department did not follow the Solicitor's opinion in levying the taxes now in dispute I do not know. When or why the Department between May and October, 1922, so radically changed its mind about how to assess mutual insurance companies under this law I do not know. But the change must have been made during these months, because by following its Solicitor's opinion there would be no surplus or contingent reserves maintained for the general use of the business upon which to assess the tax under the then existing condition of the company's assets and liabilities as shown by its Annual Reports. Therefore, the Commissioner finally concluded to throw out, and he did throw out, from the liability side of the Company's accounts; important items of liabilities, and he thereby derived a taxable sum. But the taxable sum he thus derived is both incorrectly determined, and unreasonable and prohibitive in amount.

III.

How the Commissioner Assessed the Tax.

"Every life insurance company is required by law to file annually in each state where it transacts business, in the office of the Superintendent of Insurance or other corresponding state officer having supervision of insurance, a

report showing, among other things, its income and disbursements for the preceding calendar year, which report must include a statement of its assets and liabilities (R. 45).

"Such reports are required to be made upon uniform blank forms prepared by a committee of, and adopted by, the National Association of Insurance Commissioners, and known as 'Convention Edition Form'" (R. 45).

The Commissioner took this official report and deducted from the market value of the Company's assets as shown by it certain of its liabilities. Exhibit F, commencing at page 95 and concluding on page 114, is the Annual Report from which the Commissioner derived the capital stock valuation for the year ending June 30, 1919, of $124,500,000. For the other years the capital stock value for the purpose of the tax was calculated in the same way from the Annual Reports, Exhibit G commencing on page 115, Exhibit H commencing on page 134, and Exhibit I commencing on page 154. As these exhibits are all alike except as to figures, and as the method of calculating the capital stock value was the same for each year, it will be sufficient to confine our discussion to the year ending June 30, 1919, and the method of getting at what was used as the taxable sum for that year.

Here is his calculation (R. 46),—

"Said Commissioner, in assessing said capital stock tax paid for the fiscal year ending June 30, 1919, deducted from the book value of plaintiff's 'admitted assets' as of December 31, 1917 (shown in line 47, page 4, Exhibit F) (R. 110) . . $934,929,381.52

1. The difference between the book-value and the market-value of said 'admitted assets' $50,291,672.51

2. The amount of the legal reserves as shown by items 7, 8 and 9 on page 5 of Exhibit F 734,510,999.13

3. The total of items 10 to 34, both inclusive, and items 43, 44, 45 and 46, as shown on page 5 of said Exhibit F	25,621,336.39	
4. Exemption	5,000.00	
Total deductions		810,429,008.03
Leaving a difference of		$124,500,373.49

upon which last aforementioned sum said Commissioner levied, assessed and collected said capital stock tax of $124,500 for said fiscal year ending June 30, 1919."

For the convenience of the Court I here copy in full from Exhibit F the several items in the Commissioner's above calculation the numbers only of which he gives in items 2 and 3 of his statement. They are as follows,—

"7. Net reserve (Paid-for basis) (R. 111)	$728,484,785.00	
8. Extra reserve for total and permanent disability and accidental death benefits (R. 112).....	563,494.00	
9. Present value of amounts not yet due on supplementary contracts not involving life contingencies (R. 112)	5,462,720.13	
Total		$734,510,999.13
10. Present value of amounts incurred but not yet due for total and permanent disability benefits (R. 112)	213,892.00	

11.	Liability on policies cancelled and not included in net reserve (R. 112)	467,963.84
12 to 20 inclusive.	Unpaid policy claims (R. 112)	10,350,318.67
21.	Due and unpaid on supplementary contracts *not* involving life contingencies (R. 113).....	13,849.75
22.	Dividends left with the Company to accrue at interest and accumulated interest thereon (R. 113)	2,180,726.52
23.	Premium paid in advance, including surrender values so applied (R. 113)..	1,093,413.43
24.	Unearned interest $3,129,273.54 and rent $7,607.38 paid in advance (R. 113)	3,136,880.92
25.	Commissions due agents on premium notes when paid (R. 113)	24,091.55
26.	Commissions to agents due or accrued (R. 113) ...	9,632.41
28.	Salaries, rents, office expenses, bills and accounts due or accrued (including $3,350.72 accrued charges on deposits) (R. 113)	177,424.46

29.	Medical Examiner's fees $26,908.22; Inspector's fees $5,736.90; and legal fees $4,719.96; due or accrued (R. 113)	37,365.08
30.	Estimated Amount hereafter payable for Fed., State and other taxes based upon the business of the year of this statement (including $41,370.75, accrued taxes on Interest and Deposits) (R. 113) ..	1,957,353.36
34.	Dividends or other profits due policyholders, including those contingent on payment of outstanding and deferred premiums (R. 113)	1,741,222.65
	Total	$25,621,336.39

IV.

Liability items which the Commissioner threw out, thus making a false and fictitious net value of the assets as a basis for the tax.

The Commissioner did not deduct from assets, as he should have done, the following items of liabilities as shown by Exhibit F, commencing at page 113,—

"35.	Dividends declared on or apportioned to *annual dividend* policies payable to policyholders to and including December 31, 1918, whether contingent upon the payment of renewal premiums or otherwise (R. 113)	$12,437,514.00
36.	Dividends declared on or apportioned to *deferred dividend* policies to policyholders to and including December 31, 1918 (R. 114).....	14,123,549.64
37.	Amounts set apart, apportioned, provisionally ascertained, calculated, declared or held awaiting apportionment upon *deferred dividend* policies not included in Item 36 (R. 114)	107,041,778.00."

The description of the last above three sums which the Commissioner threw out from the liability side of the Company's report of Assets and Liabilities, is in the language of the form furnished by the Superintendent of Insurance, not the language of the Company.

V.

What were these thrown-out items? Were they "surplus or contingent reserves maintained for the general use of the business" or "reserves the net additions to which are included in net income under the provisions of Title II (The Income Tax)", or were they neither the one nor the other?

They were neither the one nor the other. None of them was maintained for the general use of the business. None of them was reserves. They were each and all over-payments of premiums under a mutual insurance plan in which each insured is entitled to his insurance at cost but pays in advance an estimated sum which is reduced to cost when cost is known by returning the sum the insured paid in excess of what cost turned out to be.

Let us see more fully and precisely just what these several thrown-out items were,—

1. It is the essence of mutual life insurance on the level premium plan that each insured is entitled to receive, and must receive, his insurance at cost (R. 39). Or, as this Court put it in *Penn Mutual* v. *Lederer*, 252 U. S. 523, at page 525,—

> "It is the essence of mutual insurance that the excess in the premium over the actual cost as later ascertained shall be returned to the policyholder."

The Company collects in advance an estimated sum or level premium and adjusts this sum to cost when cost is ascertained by the accounting made at the end of each year (R. 39).

2. The Company's charter requires it to ascertain the excess in the premium over the actual cost "as soon as practicable after the 31st day of December each year" (R. 40).

How this accounting is made is shown in the record commencing at page 40. At the conclusion of the accounting the Company's directors pass appropriate resolutions for the distribution of the year's receipts properly to improve the various funds the Company is required to hold for the use of its business. What is left over and above this constitutes the excess in the premium over cost which belongs to the policyholders and must be returned to them. The directors pass appropriate resolutions for returning to the policyholders such excess in the premium in accordance with the terms of their respective contracts (R. 41, Exhibits A, B, C and D, pp. 61, *et seq.*).

3. Two plans exist under which must be returned to the policyholders the sums they paid as premium in excess of what turned out to be the cost of carrying the insurance;—one of these plans is called the annual dividend plan, the other the deferred dividend plan; but under each plan the estimated advanced premium is exactly the same; the insurance cost is exactly the same; the sum to be returned is exactly the same for each insured of the same class and equal expectation of life (R. 42, Paragraph Eleventh).

(a) A mutual life insurance company cannot discriminate between its policyholders. If it did, its business would not be mutual. Besides, the laws of New York and of practically every state provide that "No life insurance corporation doing business in this state shall make or permit any discrimination between individuals of the same class or of equal expectation of life in the amount of payment or return of premium or rates charged for policies of insurance, * * * or in the dividends or other benefits payable thereon, or in any of the terms or conditions of the policy."

New York Insurance Law, Section 89.

(b) Policies on the annual dividend plan provide for paying back to the policyholders each year their over-payments

of premiums (Paragraph Twelfth, R. 42). Policies on the deferred dividend plan provide for holding the over-payments, the amount of which the Company ascertains each year, to the credit of the deferred dividend policyholders as a class, accumulating them at interest, and paying back to each policyholder in accordance with the terms of his contract his share of the accumulated sum on the date named in his policy for doing so, usually twenty years after the insurance took effect (Paragraph Thirteenth, R. 43, *et seq.*).

(c) While the policies on these two plans differ as to the time when the over-payment of premiums shall be returned to the policyholders, they do not differ as to the sum overpaid. "The amount of divisible surplus is the same for each $1,000 of insurance on policyholders of the same age and insurance plan whether the policy is on the deferred or is on the annual dividend plan; that is, if the amount of the determined distributable surplus apportioned to the deferred dividend policyholders as a group were distributed among them for payment during the year as is done in the case of annual dividend policies, each deferred dividend policyholder would receive the same sum for each $1,000 of insurance as each annual dividend policyholder of the same age and insurance plan receives" (R. 42, Paragraph Eleventh).

4. We may now see just what these several items were which the Commissioner threw out of the liability side of the Company's account, namely,—

(a) Item 35 is the excess in the premium over the actual cost which the annual dividend policyholders paid in 1917, the amount of which the company ascertained at the accounting in January, 1918, and which in January, 1918, the Company declared as dividends payable back on the several anniversaries of their policies in 1918 to those respective policyholders from whom it received the over-payments. "These dividends were payable and the plaintiff paid them on the anniversary of each annual dividend policy whether the

premiums then due were paid or not. If the insured was then living it was paid to him; if not, then to the beneficiary named in his policy" (R. 47).

(b) Item 36 is the excess in premium over the actual cost paid by the company's deferred dividend policyholders, with interest accumulations, which, out of the total over-payments held to the credit of the deferred dividend policyholders as a class, was declared as a dividend by the Company's Board of Directors at their January, 1918, meeting, and distributed among and paid to said policyholders during the year 1918 (R. 48).

(c) Item 37 is the amount of the over-payments of premiums made by the Company's deferred dividend policyholders, with interest accumulations, which (R. 49, *et seq.*) the Company credited to such policyholders as a class, and carried to their credit in a special fund called "Interim Accumulation Fund," and is held awaiting apportionment among and payment to its deferred dividend policyholders on the several dates named in their respective policies for such payment. "Said sum of $107,041,778.00 consisted of all the accumulated credits to all the plaintiff's deferred dividend policyholders, except the accumulated credits to the plaintiff's several deferred dividend policies on which a dividend was payable during the year 1918 (Item 36), and was the balance in said accumulated deferred dividend fund after (1) adding interest to the amount of said fund held during the year 1917, and (2) merging therein the amount of the credits to the plaintiff's said deferred dividend policyholders in 1917, and (3) after deducting therefrom the total amount of the dividends payable in 1918 to the plaintiff's deferred dividend policyholders" (R. 50).

Thus was each one of these three items thrown out of the liability side of the Company's account a liability in the strictest sense. No one of them was surplus or contingent reserves *maintained for the general use of the business*, nor could it be. No one of them was reserves at all. They were each and all over-payments of premiums, which the basic

principle of mutual insurance as well as the policy contracts required the company to return to the policyholders. No part of them constituted cost of insurance. The entire amount of each of them was the sum the policyholders paid in excess of cost, to which the company had no right after the amount of the excess was once ascertained. Therefore they could not nor could any one of them be maintained for the general use of the business.

Specification of Errors Relied Upon.

The Company relies upon each of the following several assignments of error (R. 176),—

First. The Court erred in finding and adjudging that the plaintiff was liable for the payment of a capital stock tax for the year ending June 30, 1919.

Second. The Court erred in not deducting from the market value as of December 31, 1917, of the plaintiff's total admitted assets such deposits or reserve funds as the plaintiff was required by contract to hold for apportionment among and payment to its policyholders, to wit, the sum of $107,041,778.

Third. The Court erred in not deducting from the market value as of December 31, 1917, of the plaintiff's total admitted assets the dividends declared on deferred dividend policies and payable absolutely, to wit, the sum of $14,123,549.64.

Fourth. The Court erred in not deducting from the market value as of December 31, 1917, of the plaintiff's total admitted assets the dividends declared on annual dividend policies and payable absolutely, to wit, the sum of $12,437,514.

Fifth. The Court erred in not finding and adjudging that the plaintiff was entitled to refund of the entire capital stock paid by it for the period ending June 30, 1919.

Sixth. The Court erred in dismissing the plaintiff's complaint as to its First Cause of Action and in adjudging that the plaintiff was not entitled to the refund of any sum on account of said capital stock tax paid for the year ending June 30, 1919.

Seventh. The Court erred in finding and adjudging that the plaintiff was liable for the payment of a capital stock tax for the year ending June 30, 1920.

Eighth. The Court erred in not deducting from the market value as of December 31, 1918, of the plaintiff's total admitted assets such deposits or reserve funds as the plaintiff was required by contract to hold for apportionment among and payment to its policyholders, to wit, the sum of $100,893,328.

Ninth. The Court erred in not deducting from the market value as of December 31, 1918, of the plaintiff's total admitted assets the dividends declared on deferred dividend policies and payable absolutely, to wit, the sum of $19,000,738.13.

Tenth. The Court erred in not deducting from the market value as of December 31, 1918, of the plaintiff's total admitted assets the dividends declared on annual dividend policies and payable absolutely, to wit, the sum of $13,636,876.

Eleventh. The Court erred in not finding and adjudging that the plaintiff was entitled to refund of the entire capital stock tax paid by it for the period ending June 30, 1920.

Twelfth. The Court erred in dismissing the plaintiff's complaint as to its Second Cause of Action and in adjudging that the plaintiff was not entitled to the refund of any sum on account of said capital stock tax paid for the year ending June 30, 1920.

Thirteenth. The Court erred in finding and adjudging that the plaintiff was liable for the payment of a capital stock tax for the year ending June 30, 1921.

Fourteenth. The Court erred in not deducting from the market value as of December 31, 1919, of the plaintiff's total admitted assets such deposits or reserve funds as the plaintiff was required by contract to hold for apportionment among and payment to its policyholders, to wit, the sum of $88,157,964.

Fifteenth. The Court erred in not deducting from the market valne as of December 31, 1919, of the plaintiff's total admitted assets the dividends declared on deferred dividend policies and payable absolutely, to wit, the sum of $18,194,897.56.

Sixteenth. The Court erred in not deducting from the market value as of December 31, 1919, of the plaintiff's total admitted assets the dividends declared on annual dividend policies and payable absolutely, to wit, the sum of $13,850,878.

Seventeenth. The Court erred in not finding and adjudging that the plaintiff was entitled to refund of the entire capital stock tax paid by it for the period ending June 31, 1921.

Eighteenth. The Court erred in dismissing the plaintiff's complaint as to its Third Cause of Action and in adjudging that the plaintiff was not entitled to the refund of any sum on account of said capital stock tax paid for the year ending June 30, 1921.

BRIEF OF THE ARGUMENT.

I.

No Capital Stock Tax for the year ending June 30, 1921, because the Revenue Act of 1921 imposed a special income tax on life insurance for 1921 and thereafter in lieu of the Capital Stock Tax.

Section 243 of the Revenue Act of 1921 provided as follows,—

> "That in lieu of the taxes imposed by Sections 230 (The Income Tax on Corporations Generally) and 1000 (The Capital Stock Tax) and by Title III (War Profits and Excess Profits Tax) there shall be levied, collected and paid for the calendar year 1921 and for each taxable year thereafter, upon the net income of every life insurance company a tax as follows:"

And then the Act goes on to impose on life insurance a special income tax for 1921, and for each taxable year thereafter, which is to be in lieu of the capital stock tax for 1921 and of the other Federal taxes described.

This special income tax for 1921 and subsequent years was intended to impose on life insurance companies a tax the amount of which would be at least equal to all the taxes they would have been required to pay if instead of being subjected to this special income tax they had been subject like other corporations to the income tax on corporations generally, plus the capital stock tax, plus the war profits and excess profits tax. Indeed, in reporting this special income tax for passage the Congressional Committee said, after explaining it, "The new tax will yield a larger revenue than the taxes which it is proposed to replace."

Under this plain provision of Section 243 of the Revenue Act of 1921 is it according to law to impose on these cor-

porations for 1921 a capital stock tax when Congress that year imposed upon them a special income tax which was to be in lieu of the capital stock tax? Or is it fair to make them pay a capital stock tax for that year when the special income tax which Congress imposed upon them for 1921 in lieu of the capital stock tax for 1921 was designed to "yield a larger revenue than the taxes which it is proposed to replace"?

Both courts, however, have held that, notwithstanding what the Act of 1921 so plainly says, the Company is liable for the tax for the year ending June 30, 1921; but they so held on different and inconsistent grounds, and neither of them on any ground that I think is tenable.

1. The Trial Court held that the company was liable for the 1921 tax for two reasons,— First, because the express repeal of the 1918 capital stock tax by the 1921 Act did not take effect until January 1, 1922; and Second, because the 1921 Act did not become a law until November 23, 1921, and that meantime "on July 1, 1921, plaintiff came under an absolute liability to pay taxes for the privilege theretofore exercised" (R. 32).

First. As to the express repeal of the 1918 capital stock tax by the 1921 Act not taking effect until January 1, 1922.

(a) It is true Section 1400 of the Act of 1921 says that the repeal of the capital stock tax provisions of the Act of 1918 shall take effect on January 1, 1922. But has not Congress power to limit the application of a statute without formally repealing it? And when, as here, the intent of Congress is so clearly expressed, shall we say that the Act cannot have the effect intended because the old law was in force for some purpose and not formally repealed?

(b) The formal repeal of the 1918 Capital Stock Tax law is wholly immaterial to the merits of this case.

Section 243 of the Act of 1921 is a part of the income tax title of the Act of 1921. About the income tax, Section 263

of the 1921 Act says,— "This title (The Income Tax) shall take effect as of January 1, 1921."

So that on January 1, 1921, the special income tax became effective and was in lieu of the capital stock tax and of the other forms of taxation referred to in Section 243.

(c) If, however, the repeal of the 1918 Capital Stock Tax law were material here, the provisions of the Act of 1921 constitute a repeal of it as to life insurance companies.

The Act of 1921 covers the whole field embraced by the Act of 1918. It imposes an income tax, a war profits and excess profits tax, an estate tax, a capital stock tax, and the other forms of tax that the Act of 1918 imposes, and contains, without any change, most of the provisions of the 1918 Act. What new legislation this 1921 Act contains is new legislation only in so far as in substance or operation it differs from the prior law. Where, in such case, the new legislation, as here, prescribes a new method of taxing a class of corporations, the latter act repeals by implication the old law.

U. S. v. *Tynen,* 11 Wall. 88;
King v. *Cornell,* 106 U. S. 395;
Tracy v. *Tuffly,* 134 U. S. 206;
Fisk v. *Henarie,* 142 U. S. 459;
District of Columbia v. *Hutton,* 143 U. S. 18;
Gibson v. *U. S.,* 194 U. S. 182;
Rogers v. *Nashville, C. & St. L. Ry. Co.,* 91 Fed. 299;
Great Northern v. *U. S.,* 155 Fed. 945.

In the leading case of *U. S.* v. *Tynen,* 11 Wall. 88, frequently cited and always followed on this subject, the Court said, at page 92,—

> "When there are two acts on the same subject, the rule is to give effect to both if possible. But if the two acts are repugnant in any of their provisions, the latter act, without a repealing clause, operates to the extent of the repugnancy as a repeal of the first; and even

> where two acts are not in express terms repugnant, yet if the latter act covers the whole subject of the first, and embraces new provisions, plainly showing that it was intended as a substitute for the first act, it will operate as a repeal of that act."

In *King* v. *Cornell*, 106 U. S. 395, MR. CHIEF JUSTICE WAITE said,—

> "While repeals by implication are not favored, it is well settled that where two acts are not in all respects repugnant, if the later act covers the whole subject of the earlier, and embraces new provisions which plainly show that it was intended as a substitute for the first, it will operate as a repeal."

In *Rogers* v. *Nashville, C. & St. L. Ry. Co.*, 91 Fed. 299, in an opinion by CIRCUIT JUDGE LURTON, in which CIRCUIT JUDGE TAFT and DISTRICT JUDGE SEVERENS concurred, the Court said,—

> "Undoubtedly the general rule is that, when there are two acts upon the same subject, effect should be given to both if possible. This is impossible, if the two acts are repugnant in any of their provisions. The new law must, therefore, operate as a repeal of the old law, without regard to a repealing clause, to the extent of the repugnancy. Neither is it always essential that there shall be an express repugnancy between the new and old statutes. If the latter law covers the whole field embraced by the earlier act, and includes any new legislation tending clearly to indicate that the new statute was intended to take the place of the first act, it will be treated as repealing by implication the older provisions upon the same subject. It will not be presumed that the legislature intended two distinct enactments upon the same subject."

It cannot be questioned that the Act of 1921 covers the whole field embraced by the Act of 1918. It includes new legislation tending clearly to indicate that the Act of 1921 was enacted to take the place of the Act of 1918. It imposed on life insurance companies a special income tax for 1921

in lieu of the capital stock tax for 1921; the income tax provisions of the Act went into effect January 1, 1921; hence, clearly, under the authorities, the income tax provisions of the Act of 1921 superseded and in effect repealed, as to life insurance companies, all the other laws referred to in Section 243 imposing Federal taxes.

Second. As to the 1921 Act not becoming a law until November 23, 1921, and meantime the company, on July 1, 1921, becoming under an absolute liability to pay a tax for the privilege theretofore exercised.

(a) The 1921 Act did not become a law until November 23, 1921, but its income tax provisions took effect as of January 1, 1921. Therefore the effect of the Act was just the same as if it had been passed and approved January 1, 1921, or at an earlier date to take effect January 1, 1921.

Stockdale v. *Insurance Company,* 21 Wall. 323;
Brushaber v. *Union Pacific,* 240 U. S. 1;
U. S. v. *McHatton,* 266 Fed. 602.
Untermeyer v. *Anderson,* 276 U. S. 440;
Swab v. *Doyle,* 269 Fed. 325.

(b) Moreover, the 1921 Act in plain terms says that the capital stock tax provisions of the 1918 shall not be in effect as to life insurance on or after January 1, 1921.

Section 1400 (b) of the Act of 1921 says,—

> "In the case of any tax imposed by any part of the Revenue Act of 1918 repealed by this Act, if there is a tax imposed by this act in lieu thereof, the provision imposing such tax shall remain in force until the corresponding tax under this Act takes effect under the provisions of this Act."

The 1921 capital stock tax here in dispute was imposed, if at all, by that part of the Revenue Act of 1918 known as Section 1000. The special income tax imposed by the Act of 1921 on life insurance companies was in lieu of the tax

imposed by Section 1000. Hence, as to life insurance companies, the provision of the 1918 Act imposing a capital stock tax on them only remained in force until the corresponding tax under the 1921 Act, namely, the special income tax on life insurance companies, took effect. This special income tax on life insurance under the 1921 Act took effect January 1, 1921. Therefore by the plain terms of the 1921 Act the capital stock tax provisions of the 1918 Act were not in effect as to life insurance companies after January 1, 1921.

(c) But the Trial Court says (R. 32),—

> "On July 1, 1921, plaintiff came under an absolute liability to pay taxes for the privilege theretofore exercised (that is, the privilege of doing business in a corporate capacity for the year ending June 30, 1921). A statute enacted after that date might admittedly relieve it of this liability, but such a Congressional intent is not lightly to be presumed."

There are several answers to this,—

(1) The plaintiff's liability for the capital stock tax for the year ending June 30, 1921, was not absolute on July 1, 1921; it was conditional,—conditional on Congress not passing a new act imposing on life insurance companies another tax in lieu of that tax. But Congress did pass such an act and said the new tax should be in lieu of the capital stock tax and other taxes for the year 1921. Thereupon, this conditional liability became no liability.

(2) There is no virtue in the date, July 1, 1921, on which the Court says the plaintiff's liability for this tax became absolute, because the 1921 Act expressly provides for all such cases.

Section 200 of the 1921 Act relating to the income tax says,—"The first taxable year, to be called the taxable year 1921, shall be the calendar year 1921, *or any fiscal year ending during the calendar year of 1921.*" And that section

defines fiscal year as a "period of twelve months ending on the last day of any month other than December."

Suppose the fiscal year of an income tax payer ended June 30, 1921,—Would he be taxed for that year under the law of 1918? Would it be proper to say of him that he was taxed under the 1918 Act because when his fiscal year expired his net income for the year was thereby fixed, and he "came under an absolute liability to pay" an income tax under the 1918 Act? His liability for an income tax for the year ending June 30, 1921, under the 1918 Act, was, like the Company's liability for the tax in question, not absolute but conditional on the Congress not passing another act which would tax him for that year under the new Act.

Kentucky Jockey Club v. *Lucas*, 14 Fed. (2d) 539.

(3) But the Trial Court says, a statute enacted after the tax for the year ending June 30, 1921, accrued might relieve the taxpayer from such tax, but the intent to do so is not lightly to be presumed (R. 32).

We are not asking the Court to presume, lightly or otherwise, that the 1921 Act relieves the plaintiff from liability for the capital stock tax for the year ending June 30, 1921. We merely ask the Court to take the 1921 Act for what it plainly says. We ask the Court to hold that the special income tax on life insurance companies imposed for 1921 by the Act of 1921 was in lieu of the capital stock tax for 1921, or for any fiscal year ending in 1921, because the statute plainly says so. We ask the Court to hold that Section 1000 was not in effect as to life insurance companies, because the 1921 Act imposed a special income tax in lieu of the capital stock tax; that this special income tax went into effect January 1, 1921 and therefore that Section 1000 did not remain in force as to life insurance companies after the special income tax imposed by the Act of 1921 took effect January 1, 1921.

2. The Court of Appeals holds the company liable for the year ending June 30, 1921, not for any of the reasons stated

by the Trial Court, but, contrary to the opinion of the Trial Court, because the taxes "were levied in advance" (R. 191), the Department having so construed the law, and the taxes being special taxes which are "generally payable in advance under Section 186, Title 26, of the United States Code" (R. 191).

(a) The Trial Court says, "The capital stock tax payable on July first of any year was for the privilege of doing business during the year just elapsed, as is shown by the fact that corporations which had not engaged in business during the preceding year were not subject thereto, even more clearly than by the fact that its measure was the fair average value of the capital stock during the preceding year."

This seems to me to be the plain meaning of the law. The tax is an excise tax upon the privilege of doing business in a corporate capacity during the preceding year. A corporation not engaged in business during the preceding year is not taxed. A corporation commencing business, say, July 1, 1918, would then have no tax to pay. If, however, it continued business for a year then and only then would it be liable for the tax. And why? Because it had done business in a corporate capacity during the year. This was a valuable privilege and therefore taxable; and the measure of the tax was "the fair average value of its capital stock" during the period it enjoyed the taxable privilege, namely, the preceding year.

This is the only construction that can give meaning and practical effect to that clause of the law which says,— "The taxes imposed by this Section shall not apply in any year to any corporation which was not engaged in business * * * during the preceding year ending June 30th." It is the only rational construction to justify taking as a measure of the tax the fair average value of its capital stock for the preceding year. Why take the fair average value of the capital stock for the year ending June 30, 1919, as a measure of the value of exercising a corporate franchise for

the next year, the year ending June 30, 1920? There may be no relation, indeed we are now too well seeing there is no necessary relation, between the two; but between the fair average value of the capital stock during any one year and the value of doing business in a corporate capacity that same year there is a real and intimate relation.

(b) But the Appellate Court says the Department construed the law as making the tax payable in advance.

(1) Our first answer to this is, that the Department did not and could not construe the law as making the tax payable in advance by mutual insurance companies because the law had no application to them until February 24, 1919, the date of the approval of the Act, nearly eight months after July 1, 1918, the date the tax became effective.

(2) The second answer is, that there is no ambiguity in the law if meaning and effect are to be given to that part of it which says, "The taxes imposed by this section shall not apply in any year to any corporation which was not engaged in business * * * during the preceding year ending June 30th", and requires the amount of the tax to be measured by "the fair average value of the capital stock for the preceding year". It is only when a law is ambiguous that the Department's construction may have weight.

St. Paul &c. R. Co. v. *Phelps,* 137 U. S. 528;
Houghton v. *Payne,* 194 U. S. 88;
U. S. v. *Mo. P. R. Co.* 278 U. S. 269.

(3) And finally, if, as the Trial Court held, the tax payable in "any year was for the privilege of doing business during the year just elapsed", the Department could not by construction make it payable for some other year. That would be legislation, not construction.

(c) The Appellate Court's other reason for holding the tax payable in advance is, that it is a special tax and special taxes are generally payable in advance under Section 186, Title 26, of the United States Code.

The origin and history of Section 186 of Title 26 of the United States Code shows that Section 186 has no application to a special excise tax such as this.

Section 186 had its origin in the Revenue Act of 1864. *13 Statutes at Large*, Chapter 173, p. 223.

Section 72 of the 1864 Act imposed an annual license tax on a vast list of trades, businesses and professions, such as bankers, wholesale dealers, retail dealers, brokers, pawn brokers, hotels, peddlers, butchers, lawyers, and many others. These license taxes were payable annually in advance on May 1st. They were all capable of being paid in advance because the statute fixed the amount of each of them at a specific sum, such as $10, $50, $100 or other exact sum. The amount of no one of them was to be determined by a valuation and assessment after the taxpayer had carried on the trade, business or profession for a year, nor was it based on the value of the property in use for the year or on any other measures depending upon the year's experience.

The use of the word license in the 1864 Act created confusion because the state laws prohibited the carrying on of some of the occupations the Federal Government licensed, and some licensees thought that because they held a license from the Federal Government they had a right to pursue the occupation in spite of the prohibition contained in the state laws.

License Tax Cases, 5 Wall. 462.

Hence, in passing the Revenue Act of 1866 in lieu of the Revenue Act of 1864, Congress dropped the word "license" and substituted for it the phrase "special tax".

Revenue Act of 1866, 14 Statutes at Large, Chapter 184, page 198.

This was substantially all the change the 1866 Act made in this feature of the law. The special taxes in the 1866 Act were license taxes in the 1864 Act, possessing the same characteristics.

Section 71 of the Act of 1866 prohibited the carrying on of any trade, business or profession upon which a special tax was imposed before paying the tax. Section 74 provided that special taxes should "become due on the first day of May in each year, or on commencing any trade, business or profession upon which such tax is imposed."

Sections 71 and 74 of the Revenue Act of 1866 were carried into the Revised Statutes as Section 3232, which prohibits engaging in any business upon which a special tax was imposed without first paying the special tax, and as Section 3237, which provides that "all special taxes shall become due on the first day of May in each year, or on commencing any trade or business on which such tax is imposed. In the former case the tax shall be reckoned for one year, in the latter case it shall be reckoned proportionately from the first day of the month in which the liability for a special tax commenced to the first day of May following."

Section 53 of the Revenue Act of 1890 (26 *Statutes at Large*, page 567), amended Section 3237 of the Revised Statutes by changing the due date of the special taxes to which it applied from May 1st to July 1st. This Section 53 of the Revenue Act of 1890 is now Section 186 Title 26 of the United States Code.

Thus the origin and history of Section 186 of Title 26 of the United States Code clearly shows that Section 186 applies, and was intended to apply, only to such special taxes as are in the nature of a license tax, the amount of which is definitely fixed by law, and capable of being paid in advance "or on commencing any trade or business upon which such tax is imposed." Clearly the section has no application to a special excise tax such as the corporation excise tax imposed by the Revenue Act of 1909, or such as this special excise tax which is not a sum definitely fixed by law, like a license tax, capable of payment in advance "or on commencing any trade or business upon which such tax is imposed", but is an indefinite sum, the amount of which is determined after the taxpayer has been in business for a year, by a valu-

ation and an assessment of the fair average value of the capital used in the business for the preceding year.

Thus none of the grounds are tenable upon which the Company has been held liable for the year ending June 30, 1921. Besides, why not take the law as Congress gives it to us? The law says the special income tax on life insurance companies for 1921 shall be in lieu of the capital stock on them for 1921. It also says that it means by 1921 not merely the calendar year, but any fiscal year ending in 1921. Why dispute about a thing that is so plain?

II.

Where a corporation has no capital stock the 1918 Act taxes as capital stock the value of its assets over its liabilities, and as applied to this case insurance companies are no exception to this rule.

1. The Massachusetts Trusts had no capital stock. They were unincorporated associations in the nature of pure trusts or partnerships. The Commissioner taxed them under the Act "by taking the fair value of the assets of the association over its liabilities and calling the difference its capital stock", and this Court said this was the proper way to tax them.

Hecht v. *Malley*, 265 U. S. 144.

MR. JUSTICE SANFORN in delivering the opinion of the Court in that case said, at page 163,—

> "We think that in the Act of 1918, in which the tax upon an association is based upon the average value of its 'capital stock', including surplus and undivided profits, these words are not to be given a technical meaning, but should be interpreted in their entirety, and, in the absence of a fixed share capital, as equivalent to the capital invested in the business, that is, the net value of the

property owned by the association and used in its business. As was said by the Circuit Court of Appeals, *the phrase in the Statute as to 'including surplus and undivided profits puts beyond doubt the question of the congressional intent to measure this tax by business and financial realities, not by bookkeeping forms or mere names.'* And this construction is in harmony with the provisions as to the excise tax on a foreign association, which is fixed upon the value 'of the capital actually invested in the transaction of its business in the United States.'

"We therefore conclude that the Crocker Association was also subject to the tax, and that this was properly *measured by the Collector by the net value of its property*—no question being made as to the correctness of his valuation."

2. This rule, applied in the case of the Massachusetts Trusts, seems to have been substantially the rule the Solicitor of Internal Revenue thought should also be applied in taxing mutual insurance companies as is shown by his opinion dated May 1, 1922, quoted from on page 8 of this brief, relating to the method of taxing mutual insurance companies.

Internal Revenue Bulletin, Vol. 1, No. 18, May 1, 1922, page 37.

3. Mutual insurance companies are no exception to the rule that applies to the Massachusetts Trusts, except to the extent that the clause, "and any reserves the net additions to which are included in net income under the provisions of Title II", constitutes an exception.

But this clause about reserves is not material to this dispute, which relates only to dividends declared, and to overpayments of premiums which belong to the policyholders and which the Company's contracts require it to hold for apportionment among and payment to the class of policyholders from whom it received them.

Both Courts held the company liable on the ground that these sums in dispute were surplus or contingent reserves maintained for the general use of the business.

Reserves in life insurance are computed or estimated sums which are set aside to liquidate future unaccrued and contingent claims, and claims accrued but contingent and indefinite as to amount or time of payment.

In *Maryland Casualty Co.* v. *U. S.*, 251 U. S. 342, the Court defines reserves at page 350 as follows,—

> "The term 'reserve' or 'reserves' has a special meaning in the law of insurance. While its scope varies under different laws, in general it means a sum of money, variously computed or estimated, which, with accretions from interest, is set aside, 'reserved', as a fund from which to mature or liquidate, either by payment or reinsurance with other companies, future unaccrued and contingent claims, and claims accrued, but contingent and indefinite as to amount or time for payment."

The items referred to in the part of the clause commencing "any reserves the net additions to which, &c.", were all in dispute in *New York Life* v. *Edwards*, 271 U. S. 108, decided in 1926, and are the several items on the liabilities side of the Company's Annual Report (R. 112, 114) which are numbered respectively 8, 10 and 44.

4. The Commissioner's method of calculating the taxable sum indicates that he had in mind the net asset rule applied in taxing the Massachusetts Trusts. Here he took the total value of the assets. But when he came to deduct the total amount of the liabilities he saw that if he deducted all the liabilities his result would agree with the Company's return. So after long hesitation he concluded to throw out these three important items of liabilities, and thus got the enormous sum of $124,500,000 as the fair average value of the capital stock for the year ending June 30, 1919.

If the Commissioner in taxing the Massachusetts Trusts had found that the assets of one or more of them did not exceed its liabilities would the Court have approved throwing out important items from the liabilities side of the account in order to derive a taxable sum?

And then, too, the unthinkable result he thus derived. All large New York stock companies have lately mutualized. Suppose the stockholders of any one of these companies had surrendered their stock on any such basis of valuation as the Commissioner took for the imposition of this tax, what in the world would have happened? Why, the largest of all life insurance companies, the Metropolitan Life, in mutualizing in 1914 valued all its shares of stock at $6,000,000 and no more; and this is the total sum the stockholders of that great company voluntarily accepted for the surrender of all their shares.

III.

Are dividends declared, payable, and paid on the next anniversary of the policies to which they belong, surplus or contingent reserves maintained for the general use of the business?

"Maintained for the general use of the business" is the important qualifying portion of this clause of the law which was intended to define what surplus or contingent reserves Congress meant, and to harmonize Clause (c) with Clause (b). Clause (b) referred to what is popularly called surplus, which the company is required by contract to hold for apportionment among and payment to certain policyholders. Hence this phrase in Clause (c), "maintained for the general use of the business", serves the double purpose,—(1) of showing what should be taxed in a mutual company, and (2) of harmonizing Clause (c) with Clause (b).

And yet both courts, in sustaining the Commissioner's calculations, have either ignored or confused the meaning of this important limiting phrase, "maintained for the general use of the business."

Are dividends declared maintained for the general use of the business? Were they a liability that could be thrown out in calculating the net value of the company's assets? There can be only one answer to these questions; the answer is obvious. From the time these dividends were declared they became a fixed and irrevocable debt liability of the Company which it was bound to pay, did pay, and could not have gotten out of paying if it had tried. There is no theory upon which these dividend items can be thrown out in calculating the amount of the Company's surplus or contingent reserves *maintained for the general use of the business.*

Taylor on Corporations (5th Ed., Sec. 568);
Meacham on Corporations (Vol. 2, Sec. 1358);
Thompson on Corporations (Vol. 2, Sees. 2131 and 2896);
Morawetz on Corporations (Vol. 1, Sec. 445);
Marshall on Corporations (Sec. 283);
Fletcher's Cyclopedia on Corporations (Vol. 2, 1924 Supplement, p. 776);
U. S. v. *Ginsberg,* 278 Fed. 336;
Staats v. *Biograph Company,* 236 Fed. 454;
Hopper v. *Sage,* 112 N. Y. 530;
Beers v. *Bridgeport,* 42 Conn. 17;
King v. *Patterson,* 39 N. J. L. 82;
Armant v. *New Orleans,* 7 So. (La.) 35.

IV.

Are over-payments of premiums, which the company's contracts require it to hold for apportionment among and payment to the class of policyholders from whom it received them and to whose credit it holds them, surplus or contingent reserves maintained for the general use of the business?

This is the sum described in Item 37 of the Company's Annual Report, Exhibit F, page 114, as,—

> "Amounts set apart, apportioned, provisionally ascertained, calculated, declared or held awaiting apportionment upon deferred dividend polices, not included in Item 36 ..... $107,041,778.",

and a like Item 37, but less in amount, for each subsequent year (Exhibit G, p. 133, Exhibit H, p. 153, Exhibit I, p. 173,) which the Commissioner threw out of the liability side of the account in assessing this tax.

This sum is described as above in the Company's Annual Reports which are in the language of the Superintendent of Insurance, but in its accountancy system it is called (R. 50) "The Interim Accumulation Fund". Both designations, however, mean the same fund, namely, the sums paid by the Company's deferred dividend policyholders each year in excess of the cost of carrying their insurance for that year, the amount of which the company ascertained at the end of each year at the same time and in the same way that it ascertained the amount of the over-payments made by its annual dividend policyholders; and which, in amount, was the same sum (R. 42) "for each $1,000. of insurance on policyholders of the same age and insurance plan, whether the policy is on the deferred or on the annual dividend plan", but which, instead of each year returning the over-payments to the policyholders who made them, as the Company did in

the case of its annual dividend policies, the Company each year passed as a whole, into this special fund and carried as a credit to its (R. 50) "deferred dividend policyholders with interest accumulations added thereto," and held it, as its contracts required it to do, for apportionment among and payment to its deferred dividend policyholders in accordance with the terms of their several policy contracts and on the respective dates named therein for making such payments (R. 42, *et seq.*).

1. The first and controlling reason, if there were no other, why this sum should not be used in computing the tax is, because the Act itself says so in plainest terms. The Act says,—

> "(b) In computing the tax in the case of insurance companies *such deposits* and reserve funds *as they are required by* law or *contract to* maintain or *hold for* the protection of or *payment to or apportionment among policyholders shall not be included.*"

2. But both Courts say Clause (b) of the Act applies to stock companies only, not to mutual companies.

Why? The Act does not say so. The Act says,—"In computing the tax in the case of insurance companies", without any exception or word of limitation. The Court, however, in order to reach the conclusion the Court reached, amends the Act. The Court ingrafts into it an exception that is not there. By construction the Court gives the Act the meaning it would have if instead of saying what it plainly says, it said, "In computing the tax in the case of insurance companies, *except mutual companies.*" This the Court cannot do. It is amendment, not construction; a legislative, not a judicial function.

Smietanka v. *First Trust & Savings Bank*, 257 U. S. 602;
Bate Refrigerator Co. v. *Sulzberger*, 157 U. S. 1;
Commr. of Immigration v. *Gottlieb*, 265 U. S. 310;

United States v. *Missouri Pacific*, 213 Fed. 169;
Atlantic Coast Line v. *United States*, 168 Fed. 175;
Lynch v. *Alworth-Stephens Co.*, 294 Fed. 190;
Omaha Water Co. v. *City of Omaha*, 147 Fed. 1;
Wrightman v. *Boone County*, 88 Fed. 435.

Smietanka v. *First Trust & Savings Bank*, 257 U. S. 602, involved the question of the taxability under the Income Tax Law of 1913 of "income held and accumulated by a trustee for the benefit of unborn and unascertained persons." The Commissioner claimed that Congress intended by the Act of 1913 to tax citizens everywhere on income from every source, less allowed deductions; hence that the income of the trust estate in question was taxable whether the beneficiaries of the trust were unborn and unascertainable or not. In answer to this the Court said on page 605 that the Commissioner of Internal Revenue had ruled that in such case, when the beneficiary was not *in esse* and the income of the estate is retained by the fiduciary, the income was taxable and the fiduciary should pay it. But in overruling the Commissioner the Court said,—"This seems to us to graft something onto the statute that is not there. It is amendment, not construction." The Court further said that in the Act of 1913, it would have been easy to require a trustee to pay an income tax on income received by him for unborn beneficiaries, or for the estate, or for the trust, but Congress did not do so; and hence that the income was not taxable.

So here, it would have been easy for Congress to have excepted mutual insurance companies from paragraph (b), if Congress had intended to do so; but it did not do so.

In *Wrightman* v. *Boone County*, 88 Fed. 435 (C. C. A. 8th Circuit), the question was, whether or not a statute of Arkansas which prohibited the revival of judgments unless *scire facias* was issued therefor within ten years from the rendition of the judgment, applied to judgments rendered before its passage or only to judgments rendered after its passage; and because the act contained no words limiting its

application to judgments rendered after its passage, the Court held that it applied to judgments regardless of the date when rendered. The Court said,—

> "The legislature had the power to except from this broad prohibition judgments rendered before the enactment of the law, but it did not do so. The fact that it failed to make any exception raises a strong presumption that it intended to make none, and brings any exception that a court might be disposed to make into the category of judicial legislation."

And so here, Congress had power to except mutual insurance companies from the benefits of clause (b) in the act in question. But it did not do so. The fact that it did not do so shows that it did not intend to do so. Hence for the Court now, by construction, to inject into the statute an exception that Congress did not put there puts the case into the forbidden category of judicial legislation.

3. But the Appellate Court says (R. 189) "(c) was certainly intended to be the sole measure of the tax on mutual companies."

Again why? To be sure, the provision about taxing mutual insurance companies was put into (c) as an amendment;—but did this make it stand out alone as a separate method of taxation, independent of the other provisions of the section of which it forms a part? That is the function of a separate act, complete in itself, not of an amendment. The very idea of amendment is some alteration which becomes a part of the thing altered with the same force and effect as if the altered thing originally so read. The amended Act, like any other Act, is to be construed as a whole, its provisions harmonized if possible, and meaning and effect given to every part of it.

The claim, therefore, that the amendment is to be construed as if it stood alone is not good; nor will it justify a judicial amendment of clause (b) by inserting in it after the words "in the case of insurance companies" the words "except mutual insurance companies". If Congress had wanted

that exception there it would have put it there. For the Court to insert it is not merely judicial amendment but is a reflection on Congress, attributing to it a degree of carelessness the time and trouble it takes in framing these bills will not justify.

4. Let us now, for the purpose of the argument, assume that clause (b) does not mean what it says, does not apply to mutual insurance companies, is the case different? That is, is the sum in question "surplus or contingent reserves *maintained for the general use of the business*"?

(a) The laws of some of the states furnish one answer to this. For example, here is an old law of Minnesota, still in force, which shows that this sum is not and cannot be maintained for the general use of the business,—

> "Every life insurance company doing business in this state conducted on the mutual plan or in which policyholders are entitled to share in the profits or surplus shall annually apportion to such policies as a class the amount of surplus so ascertained, and carry the amount of such apportioned surplus, plus the actual interest earnings and accretions of such fund, as a distinct and separate liability to such class of policies on and for which the same was accumulated, *and no company shall or any of its officers shall be permitted to use any part of such apportioned surplus fund for any purpose whatsoever other than the express purpose for which the same was accumulated.*"
>
> *Mason's Minnesota Statutes*, 1927, Vol. 1, Sec. 3394.

(b) But the conclusive answer lies in the fundamental nature of life insurance as done on the mutual, level premium plan,—the source from which this sum comes, the persons to whom it must go, and why.

I need not say, this Court has said as clearly and forcibly as it can be put,—

"It is the essence of mutual insurance that the excess in the premium over the actual cost as later ascertained shall be returned to the policyholder."

Penn Mutual v. *Lederer*, 252 U. S. 523, 525.

Besides, we have here agreed (R. 39) that "it is the essence of mutual life insurance on the level premium plan that each policyholder is entitled to receive his insurance at cost; the company collecting its estimated or level premiums in advance and adjusting the actual cost afterwards when cost is known."

The Table Rate of Premium, or level premium (R. 40) "is the estimated sum named in the policy as premium to be paid in advance and adjusted to cost when cost is known."

An account is taken at the end of each year to find out what cost was for the year and how much each policyholder paid for the year in excess of cost (R. 42). The over-payment thus each year ascertained (R. 42) "is the same for each $1,000. of insurance on policyholders of the same age and insurance plan whether the policy is on the deferred or is on the annual dividend plan."

The over-payments of the annual dividend policyholders were paid back to them each year as a dividend (R. 47). The over-payments of the deferred dividend policyholders were credited to the deferred dividend policyholders as a class (R. 50) and (R. 42) held by the Company awaiting apportionment among and payment to its deferred dividend policyholders on the several dates named in their respective policies for paying a dividend, not maintained for the general use of the business.

Can this Court say, can anyone fairly say, that this sum in excess of the cost of insurance, so acquired by the company, so held by it, which the essence of mutual insurance as well as its contracts require the Company to return to the class of policyholders from whom it received it, is "surplus or contingent reserve *maintained for the general use of the business?*"

It is not maintained for the general use of the business; it is maintained for a specific purpose. It is not insurance cost *which alone a mutual company can maintain for the general use of its business;* it is a sum received in excess of insurance cost. It was not paid by the policyholder nor received by the company with the understanding, intention or expectation that it would be maintained for the general use of the business; it was paid and received because the successful transaction of the business required payment in advance. Hence they made a liberal estimate of the sum to be paid in advance until cost could be known, with the understanding, intention, expectation, legal and contractual obligation that the over-payment would be returned to the policyholder,—not maintained for the general use of the business. The nature of the sum is such that in the event of the insolvency or liquidation of the Company the policyholders whose over-payments made it up would be preferred creditors of the Company for the entire sum.

It is no answer to this to say that there will be no surplus or contingent reserves maintained for the general use of the business upon which to impose a tax if these items are treated as their true nature demands and the law authorizes and requires. The Company is not responsible for the extraordinary death losses that result from the epidemic that raged during some of the years in question, nor for the business conditions that depressed the value of its securities after the war. Besides, is it right that by the methods here used the Company must pay a tax based on a capital stock valuation many, many times in excess of any capital stock valuation ever before thought of for such a corporation?

In mutualizing, the Metropolitan's stockholders, as already stated, surrendered their stock for $6,000,000; the Equitable's stockholders surrendered their stock for $3,453,900. If in assessing this tax the Commissioner had recognized the plain fact that the Company had no surplus or contingent reserves maintained for the general use of the business, if he had been satisfied to take as the basis of the tax the "reserves the

net additions to which are included in net income under the provisions" of the Income Tax Law, namely, items 8, 10 and 44 in the Company's Annual Report, he would have had a lawful basis for taxation; he would then have collected a tax which bore some reasonable relation to the fair value of the capital stock of such a corporation. These items for the taxable year ending June 30, 1919 (R. 112, 114) aggregate $4,646,415, putting the Company where it belongs,—between the Equitable and the Metropolitan on the basis of the valuation upon which their stockholders surrendered their stock.

V.

The judgment as to the company's First, Second and Third causes of action should be reversed and a new trial granted.

Respectfully submitted,

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